

## **SUMMARY**

The Employee Benefits Fund is an internal service fund that is used to account for the cost of health and dental insurance (County Flex), long-term disability insurance, life insurance, and flexible benefits for the County (General Fund), Community College, Library, Economic Development, and Mental Health Authority employees and retired employees who are still participating. It is managed by the Office of Human Resources. All costs of the Fund are charged back to the users of the services provided using a chargeback system updated annually by the Budget Office working with the Office of Human Resources. Each component unit must be self-supporting within this Fund. The rates that employees are charged varies with the insurance benefits they select. At the end of each fiscal year, the fund balance lapses and is reappropriated for the next fiscal year. An actuary, Bolton Offutt Donovan, Inc., evaluates on an annual basis what the ending fund balance should be to cover unforeseen expenditures. For fiscal year 2003, they recommended an ending fund balance of \$1,370,776 and it appears that will be very close to the actual ending fund balance. Employee contributions were maintained at the FY 2002 rate even though costs are projected to increase 14.8%. As a result, the County share of health and dental costs is projected to increase by \$2.3 million or an increase of 21% over FY 2002. All expenditures from the Fund must be approved by both the Office of Human Resources and the Budget Office.

Over the four-year period FY 2000 to FY 2003, the County's General Fund contribution for employee health benefits has increased from \$8,868,708 to \$13,560,074 or \$4,691,366, which represents a 53% increase. We recommended the County establish a Health Care Affordability Committee similar to the Spending/Bond Affordability Committee to assist the County in determining alternative methods to control this escalating cost. The Administration reported that additional work performed by external consultants during the FY 2004 budget presentation (after our field work was completed) made changes to the plan after evaluating alternatives. We plan to review the work and benefit changes in the near future.

## INTRODUCTION AND SCOPE

The Office of the County Auditor has performed a review of the Employee Benefits Fund. The purpose of the review was to determine what is in the fund, what services are provided by the fund, how resources are allocated to the fund, and what expenditures are charged to the fund.

The Employee Benefits Fund is an internal service fund, therefore, all costs of the Fund are charged back to the users of the services provided following a system updated annually by the County. The purpose of the Fund is to provide a financial balancing account for employee benefit costs including health, dental and optional life insurance coverage, long-term disability insurance, and flexible spending accounts. Full-time employees receive flex cash to use toward the purchase of these benefits, to fund flexible spending accounts, and/or to receive as additional “salary.” The purpose of the flexible benefits program is to allow each employee a greater degree of choice in tailoring a benefits plan to their individual needs while, at the same time, allowing Howard County to more accurately determine the cost of providing benefits to employees. This flexible benefit program was first budgeted in FY 1992. Full-time employees hired before July 1, 1993, who do not select insurance plan benefits receive \$150 in benefit credits to use toward the purchase of a dependent care or health care spending account and/or to receive as additional salary while full-time employees hired after July 1, 1993, who do not select insurance plan benefits receive \$75 in benefit credits to use for these purposes. Part-time benefited employees may enroll in these plans but will receive no benefit credits. If additional employee contributions are required for benefit elections, they will be paid with pre-tax dollars, thereby reducing the amount of taxable income, and any changes to these benefit elections may only be made during the annual open enrollment period or within 30 days of a qualifying change in family status such as marriage or loss of other coverage. Salary earnings contributed to a flexible spending account may be used only for eligible expenses. Claims for allowed expenses with receipts are submitted to the Office of Human Resources and reimbursement is included in employee paychecks. All flexible-spending funds remaining in employee accounts at June 30<sup>th</sup> is forfeited. Employees choosing not to enroll in a County medical plan because they are covered by other health insurance are required to sign a waiver statement and provide proof of coverage from another plan.

These employees will receive \$150 monthly as a taxable cash payment unless they choose to spend it on other benefits. In FY 2003, total medical insurance premiums will range from a low of \$208.21 (\$152 of this amount is the responsibility of the employee with the balance paid by the County) for a single employee to a high of \$864.74 (\$251 of this amount is the responsibility of the employee with the balance paid by the County) for an employee with three dependents. Under the first scenario, the employee could potentially pay a total of \$2 for medical insurance coverage (\$152 less \$150 flex cash). There are other premium options in between these two extremes depending on the plan chosen and the number of dependents insured under that plan.

## **FINDINGS AND RECOMMENDATIONS**

### **Revenues**

The source of funding for this Fund comes from the County (General Fund), Community College, Library, Economic Development, and Mental Health Authority's share of insurance costs that they have agreed to pay for their employees, additional employee out of pocket health, dental, and optional life insurance costs, a return of employee flexible benefits dollars, and funds received from former employees to continue their insurance coverage under the Cobra program or as retirees. These fund sources totaled \$18,275,222 in fiscal year 2002 and \$20,882,285 is budgeted for fiscal year 2003 or an increase of 14% in one year. The required level of funding and the necessary fund balance is determined each year when preparing the budget and user County departments are charged based on a set rate per employee (\$5,868 in FY 2003) which remains the same regardless of the marital status of and benefits selected by the employee. This does not apply to the Community College, Library, Economic Development, and Mental Health Authority, however, who are billed by the Department of Finance on a monthly basis for their share of costs based on invoices received from the health care providers and who are budgeted based on experience factors that are different from the general County. During the budget process, the County works with Bolton Offutt Donovan, Inc., a health care consultant, to determine what the estimated reserve should be for the Preferred Provider Plan, Traditional +65 Plan, and the Dental Plan based on the expected self-funded claims for the coming year. The County went to a self-insurance funding method for these plans in 1993 to reduce costs. Under this method, a reserve factor is used to determine the amount of claim reserve for the next year based on expected claims for the current year. The health insurance carrier bills all claims up to a predetermined total dollar amount. The county has an excess claim policy for catastrophic illness. HMO and POS plans are fully insured and no reserve is required because the health insurance carriers will cover all claims.

Charge back amounts are withdrawn from user agency budgets on July 1<sup>st</sup> and transferred to the Employee Benefits Fund. The amount charged back for FY 2003 was \$13,495,515, which represents the County's share of health and dental insurance premiums.

We verified through the financial system and the budget backup that County agencies had budgeted correctly (\$5868 per insured employee) and that the same amount had been subsequently charged against their budget and transferred into the County's financial system to fund plan expenditures.

### Expenditures

Invoices from the health vendors are submitted for approval and payment on a monthly basis to the Office of Human Resources. These invoices indicate the required monthly deposit for the next month per the terms of the contract, total claims paid the previous month, and monthly per employee charges based on the plan selected. The subsequent month's deposit is adjusted based on the difference between total expenditures and the deposit for the prior month. Expenditures are closely monitored by the Budget Office to ensure that adequate funds are available to pay the invoices as they become due and to compare actual to budget as the year progresses. As of January 2003, the County's share of paid medical and dental insurance premiums was 54% of the fiscal 2003 budget as compared to 62% the same time last year so insurance costs are a smaller percentage of what was budgeted this year versus last year and are on track to end the year under budget. There are currently two employees budgeted in the Employee Benefits Fund at a cost of \$97,806. Other related charges, such as consulting fees, bring the total budgeted administrative costs to \$224,106 for fiscal year 2003.

### Fund Growth

#### Source of Funds

The County's General Fund contribution for employee health benefits has increased from \$8,868,708 in fiscal year 2000 to \$13,560,074 in fiscal year 2003 or a 53% increase over a four-year period. For the same period of time, contributions by the other affiliated members (Community College, Library, Economic Development and Mental Health Authority) combined has increased 75% because, as stated previously, they are charged for their share of costs based on experience factors that are different from the general County. During this same period of time, employee-related contributions to the fund (health & dental, return of health flex, optional life, cobra and retirees payments) have increased by only \$121,657 or 2.8%.

## Use of Funds

Since the purpose of the Fund is to provide a financial balancing account for health insurance revenues and expenditures and also leave a designated amount for unforeseen claims, the use of funds has closely paralleled the source of funds although there cannot be a dollar for dollar comparison as a certain amount is charged back to the agencies for their share of administrative costs and the contingency reserve. Funds are also used for long-term disability payments to current employees who have been with the County for at least (5) years and disabled for at least six (6) months (the time frequently covered by the Disability Leave Bank benefit). If they are permanently and totally disabled, they are reviewed for pension benefits and, if approved, Long Term Disability is paid as a supplement to the pension benefit up to age 65. The maximum payment is the lesser of 66 2/3% of their final pay or \$2,500/month. Payments are issued through the Payroll Dept. and a recent monthly payment indicated there were 34 Long Term Disability participants receiving a combined amount of \$18,547.26. The County also pays the entire cost of term life insurance for full-time employees equivalent to two times annual salary. Employees may purchase additional coverage through payroll deductions.

## CONCLUSIONS

Our review of this Fund has indicated that the budgeted source of funds (revenues) very closely follows the budgeted use of funds (expenditures) and the Fund will end fiscal year 2003 with revenues and expenditures in line with what was originally projected. The ending fund balance, however, was originally budgeted at \$955,164 and it now appears that it will be somewhere around \$1.3 million due to the fact that the County's share of insurance costs will be approximately \$200,000 less than budgeted and there was almost \$200,000 more in the beginning fund balance than was projected. As a result, the ending fund balance or contingency will be close to the \$1,370,776 reserve recommended by the actuaries. However, it must be noted that the County's contribution to this fund has increased \$4.7 million or 53% between FY 2000 and FY 2003 and it is anticipated that the contribution will increase significantly in the FY 2004 budget. The annual increases have not been passed on to the employees. These increases in health costs will likely continue in future years and, considering the current financial issues facing the County, will absorb a greater portion of the County's budget. Therefore, we recommend:

1. *A Health Care Affordability Committee, similar to the County's Bond/Affordability Committee, be established by the Administration to review health care alternatives for the County.*

### Administration's Response:

The Administration does not agree with this recommendation. The audit appears to have been conducted prior to the County's initiating an increase in the employee's contribution towards health insurance. Page seven of the draft audit does not recognize the initiatives undertaken to address an employee's share of health insurance. The draft does not report that for the first time in recent years the employees will be paying more "out of pocket" for health insurance and in some cases, significantly more.

It should also be noted that the County, through various plan design changes and other related initiatives, has reduced the County's increase for health insurance in FY 2004 to less than the budgeted 12% countywide; which is well less than increases in recent years when the County was picking up 100% of the increases.

Further, all labor unions have tentatively agreed to “out of pocket” health insurance increases for the employees they represent. These increases will take place on July 1, 2003; the same day that a 2% pay raise will be offset by an increase in employee premiums.

In summary, the Administration feels that it is not necessary to establish a Health Care Affordability Committee for the following reasons:

- ? Benefits are negotiated with the employee unions?
- ? The County utilizes the services of outside personnel including consultants and some well-versed employees to determine health care affordability.?
- ? There are not many, if any, health care alternatives that have not been examined.?

**Auditor’s Comment:**

Our audit work was completed before the FY 2004 Budget was approved and the Administration has made improvements in the cost sharing of health benefits cost with the employees. We also realize that the unions play a significant role in the decisions affecting health benefits. However, with the cost of health benefits escalating \$4.7 million between FY 2000 and FY 2003 (and another \$1.2 million in FY 2004), we believe that the more information the County has on health care options, the more solutions may be available for slowing this growth in health care costs. We will review the work of the outside personnel and consultants noted in the Administration’s response. After that review, we will evaluate if there would be additional value gained by establishing a Health Care Affordability Committee.

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